(10) (9)

Nos. 87-963, 87-1616

IN THE

Supreme Court of the United States

OCTOBER TERM, 1988

ROBERT L. HERNANDEZ,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

KATHERINE JEAN GRAHAM, RICHARD M. HERMANN, AND DAVID FORBES MAYNARD,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

On Writs of Certiorari to the United States Courts of Appeals for the First and Ninth Circuits

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REPLY BRIEF FOR THE PETITIONERS

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REPLY BRIEF FOR THE PETITIONERS

ARGUMENT

I. PARTICIPATION IN RELIGIOUS OBSERVANCES IN RETURN FOR FIXED DONATIONS TO CHURCHES DOES NOT CONSTITUTE THE KIND OF FINANCIAL OR ECONOMIC BENEFIT TO THE PAYOR THAT DISALLOWS OR REDUCES CHARITABLE DEDUCTIONS UNDER § 170.

The stipulations of facts in these cases established and the Tax Court found that the payments at issue here are fixed donations made by individuals to a tax-exempt church to participate in the religious observances of their faith. ¶¶ 4, 11, 15, 16, 23-26, 36, 39, 40, 42, 52, 53; JA 29-38; *Graham v. Commissioner*, 83 T.C. 575, 576, 577 (1984); Pet. App. 32a, 38a.[1] For nearly 70 years, the Internal Revenue Service (hereinafter "IRS") has allowed deductions as charitable contributions under § 170 of the Internal Revenue Code for such payments.

Here, for the first time, the Commissioner would deny deductions for contributions made by individuals solely to participate in religious sacraments. The government's brief reflects the convolutions necessary to its argument that this case is both unique and routine. The government rewrites seven decades of consistent IRS administrative practice, claiming that rulings involving a host of secular goods and services are controlling in a case involving a purely religious benefit and obfuscating IRS rulings that allow without question deductions under § 170 for payments made to churches to participate in religious services.

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[1] References in this brief are as follows: To Petitioners' Opening Brief, Pet. Br. ——; to Petitioners' Supplemental Brief, Supp. Br. ——; to the Brief for the Respondent, Gov. Br. ——; to the Brief of the American Jewish Congress and the National Jewish Community Relations Advisory Council as *Amici Curiae* in support of the Petitioners, AJC Br. ——; to the Appendix to the Petition for Certiorari in No. 87-963, Pet. App. ——a; to the Joint Appendix, JA ——.

Nowhere does the government cite a case or IRS ruling, apart from the instant litigation, where payments made by an individual to a church or synagogue to participate in religious services have been denied deduction. Nor does the government provide a principle or legal standard to which churches and synagogues and their members must hew. Instead, the government adduces a multitude of "facts" never before considered relevant, including the individual setting of the religious service, the church's methods of proselytizing, whether the religious service would have been provided without the payment, what category of persons other than the payor might be provided free services by the religion, what conduct in addition to payment is required under the religion's tenets, etc.

If the government prevails, the IRS undoubtedly will resolve such "factbound" determinations, as it has here, by adducing "facts" on behalf of those religions it favors and against those it disfavors. Such arbitrary and inconsistent treatment of worshipers is not sanctioned by the tax code and has no place in its administration.

A. The Government's Brief Rewrites History.

Petitioners' opening brief details the consistent line of IRS administrative pronouncements allowing deductions under § 170 and its predecessors for fixed payments by individuals to participate in the religious observances of their faiths. This practice of allowing such deductions accords with the language, legislative history and policies of § 170. Pet. Br. at 10-13, 32-37. *See also* Supp. Br. at 4-5; AJC Br. at 8-16. Although the government insists repeatedly that the determination of deductibility of fixed payments to churches is, and always has been, "factbound," the government cites no precedent whatsoever that disallows a deduction under § 170 for payments made solely to participate in religious services.

Each of the appellate decisions in this litigation, including those the government won, has acknowledged that a finding for the government requires a substantial

departure from prior administrative practice, one calling into question the "continuing validity" of prior rulings involving a wide variety of payments to churches and synagogues. *Hernandez v. Commissioner*, 819 F.2d 1212, 1227 (1st Cir. 1987); Pet. App. 27a. *See also* Pet. Br. 4-5, 13-14 n.11 (quoting cases). The appellate courts that have held for the taxpayers below have indicated that this case not only represents a major departure from prior administrative practice, but also is one that "has ominous implications for all religious institutions." *See, e.g., Neher v. Commissioner*, 852 F.2d 848, 857 (6th Cir. 1988) (quoting *Christiansen v. Commissioner*, 843 F.2d 418, 421 (10th Cir. 1988) (Seymour, J., dissenting)); Pet. Br. at 12-14.

The government, however, rewrites the administrative history of § 170, endeavoring to portray this case as nothing more than a routine application of well-settled principles. Gov. Br. at 38-43. In disavowing 70 years of consistent administrative practice, the government relies entirely upon cases and rulings involving benefits other than participation in religious observances, characterizes prior rulings that support the petitioners' position as "terse" and "fairly cryptic," *id.* at 40, and claims that their "infrequency and brevity . . . perhaps leave something to be desired for purposes of articulating a complete analytical framework." *Id.*[2]

The government's strained effort to deny the very existence of the long-standing IRS distinction between payments for participation in religious services and payments for financial or economic benefits is apparent in its assertion that deductibility of membership dues to a church involves "the same standards applicable to membership dues in secular organizations." Gov. Br. at 40.

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[2] The government ignores the ultimate conclusion of the 1919 IRS ruling, allowing deductions for a wide variety of payments for participation in religious services because "[i]n substance, it is believed that these are simply methods of contributing, although in form they may vary." A.R.M. 2, 1 C.B. 150 (1919) (reproduced at Pet. App. 57a).

Comparing the two key revenue rulings involving the treatment of membership dues to secular charities and religious organizations reveals the contrary. Revenue Ruling 68-432, 1968-2 C.B. 104, describes the circumstances under which membership dues to secular charities will be permitted or denied deduction in whole or in part. The ruling concludes that "payment of membership dues to a charitable organization is deductible as a charitable contribution *to the extent such payment exceeds the monetary value* of the benefits and privileges available by reason of such payment." 1968-2 C.B. 105 (emphasis added).[3] *See also* Rev. Rul. 67-246, 1967-2 C.B. 104; *United States v. American Bar Endowment*, 477 U.S. 105, 117-18 (1986).

In contrast, Rev. Rul. 70-47, 1970-1 C.B. 49, states unequivocally that "periodic dues paid to a church . . . are deductible as charitable contributions" under § 170 of the Code. There is no suggestion that participation in religious services ever entails the kind of benefit of monetary value that reduces or disallows charitable deductions.[4] As the Second Circuit stated, "the *quo* of religious experience can never be considered the equivalent of the *quid* of a money payment." *Foley v. Commissioner*, 844 F.2d 94, 97 (2d Cir. 1988), *cert. pending*, (No. 88-102). *See also Staples v. Commissioner*, 821 F.2d 1324, 1327 (8th Cir. 1987) ("Spiritual gain to an individual church member cannot be valued by any measure known in the secular realm."), *cert. pending*, (No. 87-1382).

[3] The IRS's General Counsel has indicated that the "primary objective" of this Ruling was "making it entirely clear that an appropriate portion" of membership dues *are deductible* to the extent the amount of such payment exceeds "the total *monetary value* of all the potential return benefits thereby obtainable." G.C.M. 33797, Apr. 15, 1968 (emphasis added). Notwithstanding its claim that the same standards apply, the government clearly departs here from the principles of Rev. Rul. 68-432. Recognizing that a determination of "the monetary value" of the benefit from religious services would be both impracticable and unconstitutional, the government insists that the amount of payment itself determines the monetary value of the religious services provided in return. Gov. Br. at 34 n.14 & 35-36.

[4] The government also relies upon Rev. Rul. 77-160, 1977-1 C.B. 351 (described as "a subsequent ruling in a related context") for its claim that deductibility of membership dues of churches and secular charities is determined by the "same standard." Gov. Br. at 40. That ruling, however, addresses the issue whether payment by a private foundation of a "disqualified person's" church membership dues constitutes an act of "self-dealing" under § 4941(d)(1)(E) of the Internal Revenue Code. The ruling held that the foundation's payment of the membership dues conferred a "*direct economic benefit*" by relieving the person from a *financial* obligation he otherwise would have incurred himself. Rev. Rul. 77-160, 1977-1 C.B. 351 (emphasis added).

General Counsel's Memorandum 36784, July 9, 1976, which analyzes this ruling in detail, notes that the membership dues at issue entitled the member to tickets for admission to "special worship services" on "certain days of special religious significance," adding "[a]s a practical matter . . . members and visitors obtain tickets under the congregation's prescribed procedures [that require payment of an 'established fee'] and display such tickets upon entering the house of worship on the days in question." The G.C.M. distinguishes explicitly the non-economic benefit of attending worship services from the *financial* benefit of a third party's payment of dues and indicates that the payments for membership dues would be deductible under § 170 if paid by the individual himself, thereby contradicting the point for which the ruling is advanced by the government.

The government also looks for support in cases involving old-age homes, sewing machines, and insurance, and principally in IRS disallowances, at least in part, of deductions under § 170 for payments for education at religious schools. Gov. Br. at 19-21, 38-39. This Court, however, has recognized the distinction in the tax law between educational activities and religious services.[5] *See Bob Jones Univ. v. United States*, 416 U.S. 574, 604 n.29 (1983) ("We deal here only with religious *schools*

[5] As petitioners' opening brief makes clear, disallowance of charitable deductions for tuition at religious schools is necessary to preclude deductions for otherwise explicitly nondeductible personal education expenditures, a problem that simply does not occur with respect to deductions for a church's provision of religious services. Pet. Br. at 32-37.

not with churches or other purely religious institutions . . . .") (emphasis in original). The IRS also is acutely aware of the distinction. *See, e.g.*, G.C.M. 35986, Sept. 13, 1974 (distinguishing religious education from religious services, explaining that religious schooling is significantly different than "an inherently religious program").

Ironically, three weeks after the government filed its brief denying the existence under § 170 of any IRS administrative practice distinguishing religious education from religious observances, IRS Assistant Commissioner Robert I. Brauer released a "question and answer guidance package" concerning deductibility under § 170 of various payments to tax-exempt charitable organizations. Commissioner Brauer indicated that this informal guidance "represents the Service's cumulative position." Question and Answer Number 10 addresses payments such as those at issue here. It refutes explicitly the statements and analysis of the government's brief and fully supports petitioners' position:

> Q10: May a taxpayer deduct payments that are solicited by religious organizations for religious and related services?
>
> A10: Deductibility depends upon the type of services provided by the religious organization. For example, parochial school tuition payments are not deductible as charitable contributions because the payments are made with the expectation of a *definite economic benefit. In contrast to tuition payments, religious observances generally are not regarded as yielding private benefits when attending the observances. The primary beneficiaries are viewed as being the general public and members of the faith. Thus, payments for saying masses, pew rents, tithes, and* ***other payments involving fixed donations for similar religious services, are fully deductible contributions.***

IRS Official Explains New Examination-Education Program on Charitable Contributions To Tax-Exempt Organizations, B.N.A. Daily Tax Report for Executives, J-1, J-3 (Sept. 26, 1988) (emphasis added).

This recent reaffirmation by the IRS of the deductibility of payments to churches to participate in religious services, first announced in A.R.M. 2, 1 C.B. 150 (1919) and reaffirmed in Rev. Rul. 70-47, 1970-1 C.B. 49, belies the government's extraordinary efforts to reinterpret seven decades of consistent IRS administrative practice. It proves false the government's claim that "[t]here is no administrative practice recognizing that payments made in exchange for religious benefits are tax deductible." Gov. Br. at 16. To the contrary, the IRS always has allowed deductions under § 170 for fixed donations made by individuals to their churches and synagogues to participate in the religious services of their faith. *See Neher*, 852 F.2d at 856-57; *Foley*, 844 F.2d at 96; *Staples*, 821 F.2d at 1326. Only Congress may reverse such a long-standing interpretation of the tax laws.

Further, the government quotes but then ignores the legislative history of § 170, and avoids altogether similar statements in IRS regulations, rulings and other administrative pronouncements that charitable deductions under § 170 are disallowed only when the donor receives a *financial* or *economic* benefit commensurate with the amount contributed. Gov. Br. at 19. *See* Pet. Br. at 32-33; AJC Br. at 8-12. The government's proposed reversal of seven decades of consistent administrative practice has no grounding in the statute, in its legislative history, in IRS regulations or other rulings, in prior judicial precedents or in the policies of § 170 of the Code. It represents an effort by the IRS to obtain unfettered discretion to allow deductions for payments to those religious organizations it favors, while disallowing them to those it disfavors.

B. The "Factbound" Inquiry Proposed By The Government Is Not A Legal Standard; It Is A License Granting Unfettered Discretion To The IRS.

1. *The Government Is Bound By Its Stipulations Below.*

Throughout its brief the government maintains that deductibility of payments to participate in religious ser-

vices is a "factbound" inquiry, one that depends on each case's "facts and circumstances." *See, e.g.*, Gov. Br. at 19, 20, 32, 41. The government then selectively recites 'facts" both to argue for its claim that the fixed donations at issue here are not deductible and to try to distinguish related practices in other faiths. Many of these "facts" are adduced to diminish the force of the government stipulations below and thereby deflect this Court from the basic legal issue of this case and, at the same time, to induce prejudice against the Church of Scientology's fund-raising methods and religious practices.

First, the government stipulated that the Scientology organizations that received the payments at issue here are tax-exempt churches eligible to receive deductible contributions under § 170(c)(2). ¶¶ 52-53, JA 38. As the government's brief recognizes, "[a]ll of the organizations listed as eligible donees in Section 170(c)(2) are obliged to operate for 'charitable purposes' and to put the public interest above the private interest. . . ." Gov. Br. at 30. Therefore, the government's claims that this Church operates as a "commercial enterprise" predominately to "make money" or provide "private benefits" to its members are directly contradicted by its stipulations. *See Neher*, 852 F.2d at 850; *Staples*, 821 F.2d at 1326.

Second, the government agreed below both that Scientology is a religion, and that "[e]very Auditing session is structured and conducted in exact accordance with rituals, codes, doctrines and tenets of Scientology." ¶ 15, JA 31. The government also stipulated that "[n]o subject matter is taught, studied, or learned during an Auditing session . . . ." ¶ 23, JA 35. The Tax Court found the payments were made for religious services, 83 T.C. at 577, Pet. App. 38a. Uncontradicted testimony demonstrates that Scientologists believe that the spiritual benefits derived from their religious practices of auditing and training accrue not only to the individual but also to the public at large. JA 40-42, 48, 53, 60-61, 66-67, 70-71. Scientologists believe that the enhancement of civilization is linked to their spiritual goals and practices.

Foley, 844 F.2d at 96. Like adherents of other religions, the fixed donations of Scientologists provide them with the opportunity to travel the spiritual path of their faith, nothing more and nothing less.

2. *The "Quid Pro Quo" Label Does Not Determine Deductibility Under § 170.*

The government attempts to conceal the discretionary nature of its position by endless repetition of the phrase "*quid pro quo*." (This phrase appears 74 times in the government's brief.) As the history of § 170 makes clear, however, the charitable process is suffused with *quid pro quo*'s. Benefits virtually always flow from charitable contributions, including those to religious organizations. Churches and synagogues that require fixed payments from their members typically promise them a better life here on earth and, frequently, salvation. Treating participation in religious observances as the kind of benefit that requires disallowance of charitable deductions would frustrate Congress' intention to allow members of all faiths to provide financial support to their churches through tax-deductible payments.

The phrase "*quid pro quo*" is only the beginning of an inquiry into the deductibility of donations to charities, an inquiry that in the secular context concerns the nature and value of any benefits provided by the charity in return for the payment. The government here instead advances the *quid pro quo* phrase to end the inquiry under § 170, and rejects the standard investigation of the value of financial or economic benefits provided to donors by secular charities.[6]

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[6] The disallowance of all or a portion of claimed deductions to secular charities is typically grounded on the following two-part test: "First, the payment is deductible only if and to the extent it exceeds the market value of the benefit received. Second, the excess payment must be 'made with the intention of making a gift.'" *United States v. American Bar Endowment*, 477 U.S. at 117-18 (citing Rev. Rul. 67-246, 1967-2 C.B. 104, 105) (quoted in Pet. Br. at 38). The government, however, regards neither of these standard tests as applicable to the instant case, contrary to its

Nowhere, however, does the government offer a "line" —a legal principle—that would enable a church or synagogue and its members to know whether (or to what extent) their payments are deductible. Instead of following the IRS practice of seven decades—allowing deduction under § 170 for payments to churches to participate in religious observances without regard to the form of the payment or the nature or value of the religious service—the government simply claims the issue is "factbound" and advances an endless litany of "facts."

Yet at issue here is the question of deductibility under § 170 of payments, fixed in amount by the church, made by its members to a tax-exempt church for the sole purpose of enabling them to participate in the religious observances of their faith. None of the "facts" adduced by the government supports disallowance of deductions for these donations.

C. "Facts" Recited By The Government Provide No Support For Its Position.

The government does not deny that individuals commonly deduct under § 170 a wide variety of fixed payments to their churches and synagogues and have done so for decades without question by the IRS. Nor—with the exception of payments made for services routinely provided in the secular realm, such as for education or parties following religious ceremonies—does the government

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assertion that "the *quid pro quo* inquiry does not differ . . . regardless of whether the particular benefits received in exchange for the payments are religious in nature." Gov. Br. at 49-50. First, the government apparently agrees with petitioner that the donor's intent is irrelevant under § 170 where payments for religious services are involved. Pet. Br. at 38 n.53. The subjective intent of petitioner Hernandez has never been placed in issue. JA 145; Gov. Br. at 6. Second, the government maintains that valuation of benefits is not appropriate for participation in religious services. Gov. Br. at 34 n.14. Thus the crucial factual determination in all other contexts—the comparison of the monetary value of the benefit provided by the charity with the amount of the donor's payment, the relationship of the *quid* to the *quo*—would be inapplicable when payments for religious services are involved. *See* Pet. Br. at 37-40.

describe even one instance where such deductions have been challenged by the IRS. Apparently, no controversy over deductibility of such payments has previously occurred.

The government nevertheless now claims that fund-raising practices of different religions "have not been *passed upon* by the IRS," and remarks that some fund-raising practices "seem clearly to yield deductible contributions, some may be 'close to the line' . . . and some may not yield deductible contributions." Gov. Br. at 42 (emphasis added). A clearer threat to fund-raising practices of mainstream churches and synagogues is hard to imagine. Deductibility, according to the government, now would turn on "the facts surrounding the payments" as "developed in an appropriate setting," with the IRS enjoying its usual presumption of correctness. *Id.*[7]

The government nonetheless attempts to limit the scope of its position, reciting various facts in an effort to explain why members of this church have been singled out for disallowance of deductions. These facts fall into four categories: (1) the individual rather than congregational nature of the religious practices at issue here; (2) the use of "commercial" or "business" techniques in fund-raising and proselytizing; (3) the form or "structure" of the transactions; and (4) miscellaneous facts offered in an effort to distinguish the fund-raising practices of mainstream religions. None of these facts supports the denial of the deductions at issue here.

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[7] In a related context, this Court described the "facts and circumstances" inquiry whether a payment is a gift under § 102 of the Internal Revenue Code as "based ultimately on the application of the fact-finding tribunal's experience with the mainsprings of human conduct to the totality of the facts of each case." *Commissioner v. Duberstein*, 363 U.S. 278, 289 (1960). This seems to be what the government is urging here. The variety and *ad hoc* quality of results under such a "factbound" test is not appropriate in determining when an individual's payments to a church or synagogue will be deductible under § 170.

1. *Individual Versus Congregational Worship.*

The government's brief demonstrates unequivocally the IRS's intention to disallow deductions for payments for Scientology religious services because they are conducted individually rather than congregationally. It was settled below by stipulation that auditing is a ritualistic religious practice. ¶¶ 15, 16, 17; JA 31. Nevertheless, the government stresses repeatedly that auditing is conducted in an individual rather than a congregational setting, Gov. Br. at 3, 5, 16, 44, and describes "the provision of individualized services" as a "hallmark" of this church's practices. *Id.* at 44.

The government claims that the IRS has made a "fact-bound" determination that masses or other "similar religious observances" provide only "incidental" benefits to the individual and "spiritual benefit to all the members of that faith and to the general public," but that "it is not apparent that an auditing session for a particular individual was believed to yield any significant benefits to other members of the Church." *Id.* at 32 (quoting Rev. Rul. 71-580, 1971-2 C.B. 235, 236). The government ignores the uncontradicted testimony that Scientologists, like adherents of other faiths, believe that the general public as well as other Scientologists benefit from their religious practices. *See, e.g.*, JA at 40-42, 48, 53, 60-61, 66-67, 70-71. As the Sixth Circuit stated in *Neher*, the attempted distinction between individual and congregational worship is "without meaning." 852 F.2d at 857. *See also Staples*, 821 F.2d at 1326 ("The public benefit from religion remains and predominates regardless of whether church doctrines provide for traditional congregational worship or individual worship as in Scientology . . . ."); *Hernandez*, 819 F.2d at 1227 ("The IRS found significance in the fact that unlike collective worship services . . . [these religious] services are performed in private sessions . . . . [T]he collective or individualized nature of those services is irrelevant . . . ."); Pet. Br. at 15-17.

The government also frequently repeats that Scientologists receive personal benefits from their participation in this Church's worship services. Gov. Br. at 4, 14, 15, 23, 24, 31, 32, 41, 43. But many faiths hold that faithful observance and worship will provide personal benefits, commonly including peace of mind, ability to cope with stress, and even increased prosperity and health. The Mormons, for example, have advertised in *Reader's Digest* that their religious services offer prospects for greater individual security and self-reliance, more satisfying personal lives, good health, better marriages and better relationships with children. *Reader's Digest*, Apr. 1978 (8 pages between 48 & 49); June 1978 (8 pages between 188 & 189); Sept. 1978 (8 pages between 64 & 65); Dec. 1978 (8 pages between 64 & 65); July 1979 (8 pages between 16 & 17). Many other churches believe in doctrines such as "seed faith," "100-fold return," "the law of sowing and reaping," and the "law of reciprocity," all of which promise rewards for participation in the faith.[8] The fact that Scientology promises benefits to the everyday lives of its members does not distinguish it from other denominations.

Whether religious observances are conducted in individual settings or in the congregational fashion of most Western religions is irrelevant to the tax treatment of fixed donations made in return for participation in those services. Neither the Internal Revenue Code nor its policies remotely suggest that such a distinction should be drawn. Furthermore, such a distinction would advantage

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[8] *See, e.g.*, O. Roberts, *Seed Faith Scriptures* (1972); P. Cho, *Salvation, Health, Prosperity* (1987); R. Kendall, *Tithing: A Call to Serious Biblical Giving* (1982). Dean Kelley in *Why Churches Should Not Pay Taxes* 52 (1977) explains that religious belief and worship are a potent stabilizing influence in the lives of church members, and often produce substantial betterment in their psychological and financial situations: "[A]n effectively functioning religion helps its adherents to cope with their life-situations, to bounce back from difficulties with resilience and confidence restored. Often a by-product of religion's stabilizing effect is that its adherents rise in socio-economic scale and become 'haves' themselves."

or disadvantage individuals based upon the religious tenets of their denomination in contravention of the First Amendment.[9]

2. *This Church's Use Of "Commercial" Or "Business" Methods In Proselytizing Its Religion Is Irrelevant.*

The government argues repeatedly that the active promotion of Church worship services, coupled with the use of business terminology and methods, is evidence that auditing is a commercial product. Gov. Br. at 4, 5, 13, 14, 22, 24, 25, 27, 35. This argument is erroneous, given that the government has conceded that the Church of Scientology is a "religion" and a "church" within the meaning of § 170 and that the fixed donations at issue here were made to participate in a religious observance. *See* Pet. Br. at 26-27 & n.37. *See also Neher*, 852 F.2d at 850 (Tax Court finding that the Church "operates in a commercial manner in providing these religious services" is "irrelevant and not controlling"); *Staples*, 821 F.2d at 1325 ("The tax court . . . ignored the fair impact of the government's stipulations.").

The government's claim that aggressive promotion of religious services transforms them into a commercial product elevates semantics over substance. Many religions "promote" their faith, through advertisements, market research, door-to-door solicitations, and countless other means.[10] Contrary to the government's suggestions,

[9] Settled religious practice, for example, of the Roman Catholic and Episcopal traditions has for centuries included the practices of individual confessions and "spiritual direction." *See* Pet. Br. at 15-17 & nn.15-16.

[10] Modern business techniques, including business terminology and promotional methods, have been used by many American religious groups for well over a century. *See* W. McLoughlin, Jr., *Modern Revivalism: Charles Grandison Finney to Billy Graham* 166-216 (1959). Indeed, the use of business techniques and terminology in proselytization is common among contemporary religious groups, including mainstream denominations. *See, e.g.*, Sellers, *Market Research and the Local Church*, Ministries Today, Sept./Oct. 1988, at 58; Goldman, *Archdiocese Tries Market Research*, New York Times, June 20, 1986, at B-3; Alsop, *Advertisers Promote Religion in a Splashy and Secular Style*, Wall Street Journal, Nov. 21, 1985, at 33; Yao, *Big Pitch for God: More Churches Try Advertising in Media*, Wall Street Journal, Dec. 31, 1979; Stiansen, *Thou Shalt Advertise*, Adweek, May 5, 1986 at 34; Maloney, *How Churches Try to Woo the Yuppies*, U.S. News & World Report, Aug. 26, 1985, at 64.

this Church is certainly not unique in "seeking to make [its religious] services attractive to persons having no prior connection to or involvement with the Church." Gov. Br. at 23.

The commonly used term for such promotion of religion is proselytization. Proselytizing is a well-recognized form of religious activity and does not transform a tax-exempt church into a commercial enterprise. *See Staples*, 821 F.2d at 1326-27 (quoting *Murdock v. Pennsylvania*, 319 U.S. 105, 111 (1943)).

3. *The Form Of The Transaction.*

The government stresses the "form" of the transactions at issue. For example, the government recites that the "Church offered a 5% advance payment discount" (Gov. Br. at 23); that the Church encouraged members to "'buy training and processing'" (*id.* at 25 n.13); that "'Customer's Order' forms" recorded fixed donations as "'sale[s]'" (*id.* at 26); and that one of the petitioners whose cases were tried below received a "'billing'" for auditing sessions (*id.*). The government also makes much of the fact that this Church sometimes makes refunds.[11] *Id.* at 4. This litany emphasizes the "form" or

[11] The issue of refunds for auditing sessions that are paid for, but not taken, was also emphasized by the Ninth Circuit in *Graham*, 822 F.2d at 849 ("[T]he right of refund if the service was not performed . . . underscore[s] that the payment matched, with some precision, the benefits to be received."). As illustrated by church law associated with Mass stipends, however, the availability of refunds may be a complicated matter of doctrinal interpretation rather than indication of a commercial transaction. *See* C. Keller, *Mass Stipends* 81-82 (1925) ("[I]t seems that according to Canon law the giver of a [Mass] stipend has a right to demand either the

"structure" of the transactions. IRS interpretations of § 170, as with other provisions of the Internal Revenue Code, heretofore have turned on the substance, not the form, of the transaction.[12] *See* Pet. Br. at 30-31; *Staples*, 821 F.2d at 1327 (quoting *Oppewal v. Commissioner*, 468 F.2d 1000, 1002 (1st Cir. 1972)) (classification of a payment depends upon more than the bookkeeping methods used by the charitable institution).

This Court, likewise, has long recognized that tax consequences turn on substance, not form—that the underlying essence of a transaction determines its taxability. *See, e.g., United States v. Phellis*, 257 U.S. 156, 168

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money or the celebration and application of a Mass.") (citing Canon 829) (footnote omitted). Refunds have also been considered, and sometimes offered, by other denominations. *See, e.g., St. Petersburg Church Offers a 'Money Back Guarantee'*, St. Petersburg Times, June 1, 1988 at 4 (Reformed Episcopal church will refund donations if contributors "feel they have not gained spiritually" from attending worship services). The decision whether or not to offer refunds is a matter for internal church policy. *Cf.* 2 National & International Religion Report, No. 12 at 4 (June 20, 1988) (Permanent Judicial Commission of Presbyterian Church considered and rejected members' claim to refund based on disagreement between members and session, on ground that individuals may not dictate the manner in which a session discharges its responsibilities).

[12] In 1919 the IRS emphasized this point, stating "In *substance*, is believed that [pew rents, assessments, church dues and the like] are simply methods of contributing, although in *form* they may vary." A.R.M. 2, 1 C.B. 150 (1919) (emphasis added).

To take but two other examples, Rev. Rul 67-246, 1967-2 C.B. 104, the key IRS administrative pronouncement regarding deductibility under § 170, considers a variety of payments by taxpayers in connection with a number of common fund-raising techniques. In detailing its guidelines for deductibility through thirteen separate examples, the IRS invariably looked to the substance, not the form, of the transaction. The IRS's most recent application of the principles announced in that ruling, Rev. Rul. 86-63, 1986-1 C.B. 88, addresses four specific fact situations in which contributions to athletic scholarship programs provide taxpayers preferred seating at athletic contests. In each case the IRS looked to substance rather than the form of the transaction in determining the amount of allowable deduction.

(1921) (treating the superiority of substance over form as well-settled in tax adjudication). The substance of the transaction at issue here—a payment made by taxpayers to enable them to participate in the religious sacraments of their faith—is an extremely common one, one that has never before been disallowed deduction under § 170.

4. *Other "Facts" Advanced By The Government In An Effort To Distinguish Other Religions Merely Confirm The Unprincipled Nature Of The Government's Position.*

The government apparently agrees with petitioners that whether the amount of a donation is set by the Church or the donor is not controlling and advances other factual distinctions among religions to limit the disallowance of deductions to members of the Scientology Church. The government, for example, advances the following facts as important in determining deductibility under § 170: (1) whether the religious service "would be said anyway without the payment" (Mass stipends); (2) the nature of "worthiness" standards that—in addition to the required payment of a fixed sum—enable the member to participate in sacraments (Mormon tithes); (3) whether fixed payments are tied to financial status (Temple dues); and (4) whether "arrangements" are made "for people of limited means" to participate in the religious service (Jewish High Holy Day tickets). Gov. Br. at 43-44.

These claimed distinctions not only are irrelevant under § 170, but also sometimes are based upon erroneous premises. Mass stipends, for example, are often given for Masses said specifically for the purpose specified by the donor. *See, e.g.*, Coriden, Green & Heintshel, *The Code of Canon Law: A Text and Commentary* 669 (1985) (Canon 948: "Separate Masses are to be applied for the intention for which an individual offering, even if small, has been made and accepted."). Likewise, although the government claims otherwise (Gov. Br. at 4 n.3), the record shows that auditing is provided free by

the Church of Scientology to members in crisis situations, due, for example, to alcohol or drugs. Pet. Br. at 7; *Church of Scientology of Calif. v. Commissioner*, 83 T.C. 381, 424 (1984). Contrary to the government's implicit suggestion, the tax code does not distinguish among religions based upon whether they provide specific benefits to addicts or indigents.

Further, the fact that observant Mormons abstain from alchohol does not in any way reduce the "inflexibility" of the connection between tithing and Temple recommends. Tithing is mandatory; without it Mormons are not admitted to the Temple even if they abstain from using alcohol. *See* Church of Jesus Christ of Latter-Day Saints, *General Handbook of Instruction* 10-1 (1985). The government also defends deductibility of Mormon tithes stating that "unlike the payments here, tithing is not a 'ticket' to a Temple recommend." Gov. Br. at 44. Of course, it must then find other "facts" to defend deductibility of "tickets" to Jewish High Holy Day services. *Id.*

The payments to mainstream religions discussed by the government, like those at issue here, are fixed in amount by the church or synagogue and entitle the payor to participate in religious services of his or her faith. In the government's repetitive trope, the "*quid*" and the "*quo*" of each of the transactions are the payment of fixed donations and participation in religious services, respectively. If the IRS is permitted—as the government insists is its right—to pick and choose among various "facts" to select which payments are deductible and which are not, discrimination against new and unfavored religions is inevitable.

II. THE DECISIONS BELOW VIOLATE THE RELIGION CLAUSES OF THE FIRST AMENDMENT.

Rather than facing squarely the impairment of religious liberty created by the IRS's attempt to deny deductions in an arbitrary and inconsistent manner, the government argues only that the government has a "compelling interest" in a sound tax system. This unremarkable statement is not disputed by the petitioners. Indeed, as pointed out in petitioners' brief, the soundness of the nation's tax system will be *undermined*, not bolstered, by the disallowance of the deductions at issue here. Pet. Br. at 48 n.62.

The IRS's proposed departure from its long-standing practice of allowing charitable deductions for fixed donations to churches in return for participation in religious services unconstitutionally will entangle the government in religious practices[13] and will create denominational preferences. *Larson v. Valente*, 456 U.S. 228 (1982); *Walz v. Tax Commission*, 397 U.S. 664, 674 (1970); Pet. Br. at 37-49.

Furthermore, as the government acknowledges, denial of a deduction for the contributions at issue here would place a governmental burden on the free exercise of petitioners' religion. Gov. Br. at 48. At the same time, the government claims, analogous fixed donations to other religions would remain deductible. Yet, rather than address this disparate treatment of religions, the government asserts merely that "even-handed administration of the tax laws" outweighs virtually any burden on religion. Gov. Br. at 48. This argument is unpersuasive in these

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[13] The government cites *Tony & Susan Alamo Foundation v. Secretary of Labor*, 471 U.S. 290 (1985) for the proposition that "administrative contact [between government and religion] does not ordinarily raise First Amendment concerns." Gov. Br. at 49. In that case, however, the Court expressly distinguished the minimum wage and reporting requirements imposed on all business employers from the unconstitutional entanglement that would result from similar requirements being placed on "evangelical activities" or other exclusively religious conduct. 471 U.S. at 305. Because the instant cases involve religious activity, the prolonged and invasive inquiries that would be necessary to value religious services or to develop other "appropriate" facts concerning the challenged church's fund-raising and other religious practices constitute precisely the kind of entanglement warned against in *Tony & Susan Alamo Foundation*.

cases.[14] Here, "even-handed administration of the tax laws" demands that fixed donations for auditing or training be allowed deduction like similar payments for other religious services, such as Mormon tithes, Mass stipends, and High Holy Day tickets.

CONCLUSION

The judgments of the Courts of Appeals should be reversed.

Respectfully submitted,

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[14] The invocation of *United States v. Lee*, 455 U.S. 252 (1982), Gov. Br. at 48, does not meet the burden of showing a compelling interest and a narrowly tailored infringement of religion. Two vital differences distinguish this case from *Lee*. First, § 170 already provides for deductions for contributions to religious organizations. Indeed, the tax code in many places treats religion specially. *See* AJC Br. at 9 n.2. Second, such deductions have always been allowed in the past, and, rather than undermining the administration of the tax system, they have proved easy to administer and even-handed among religions. The compelling interest in uniform and efficient functioning of the social security system was the basis of the Court decision in *Lee*; in the instant cases, similar donations have uniformly been permitted deduction. Consistent and efficient functioning of the tax system, therefore, dictates that the petitioners' contributions be held deductible.